96-65

MEETING THE CREDIT NEEDS OF MINORITY COMMUNITIES

HEARING

BEFORE THE

SUBCOMMITTEE ON
DOMESTIC MONETARY POLICY

OF THE

COMMITTEE ON
BANKING, FINANCE AND URBAN AFFAIRS
HOUSE OF REPRESENTATIVES

NINETY-SIXTH CONGRESS

SECOND SESSION

NEWARK PUBLIC LIBRARY

MAY 29, 1980

NOV 3 1980

Serial No. 96-65

U. S. GOVT. PUBS.
DEPOSITORY 376

Printed for the use of the
Committee on Banking, Finance and Urban Affairs

U.S. GOVERNMENT PRINTING OFFICE
65-868 O WASHINGTON : 1980

Y4.B22/1:

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MEETING THE CREDIT NEEDS OF MINORITY COMMUNITIES

THURSDAY MAY 29, 1980

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON DOMESTIC MONETARY POLICY,
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS,
Washington, D.C.

The subcommittee met at 10 a.m. in room 2128, Rayburn House Office Building, Hon. Parren J. Mitchell (chairman of the subcommittee) presiding.

Present: Representatives Mitchell, D'Amours, and Paul.

Chairman MITCHELL. Good morning. This hearing will now come to order. Those of you in the audience are fully aware of the vagaries of the Hill and the conflicts in scheduling. There are three or four meetings going on simultaneously this morning. Some of the other members of the subcommittee will be joining us, but I certainly do not want to delay the hearings to wait for them.

Today the Subcommittee on Domestic Monetary Policy is meeting for a hearing on the credit needs of minority communities and enterprises.

The smooth functioning and growth of our economy depends crucially on the growth and continuity of credit, both in-the-large and to the economy's many diverse sectors and communities. Minority communities cannot be excluded from credit markets. Minorities must have access to business and consumer credit to become full working, contributing, and sharing partners in the American economy.

The events of recent months highlight the importance of the continuity of credit flows. Between mid-February and the end of March, interest rates skyrocketed, and the flow of credit slowed to a trickle. All or nearly all sectors of our economy were quickly impacted. Housing starts and sales, and automobile production and sales dropped precipitously. The word "depression" best describes what has happened in these industries.

Fortunately, since the end of March, interest rates have fallen sharply. Some rates are now below levels of 1 year ago, and the total flow of credit has risen somewhat. Further improvement, on both fronts, can be expected if the Federal Reserve succeeds in hitting its money growth targets, even if it does so by wiggling around the target range rather than staying inside it at all times. Although the latter would be preferable, for the Fed to stay within the target ranges, moving the volume of money from over to under and from under to over the target range with short, quick, irregular movements is far preferable to veering off in one direction or another for long periods of time before taking corrective action. By wiggling around the target,

the Federal Reserve will promote longrun economic stability and the achievement, hopefully, of full employment without inflation. However, the problem of assuring adequate and continuous credit flows to minority communities and enterprises remains.

Even as interest rates were dropping and credit flows were rising in April, the Federal Reserve moved to provide small banks with special help to meet the credit were made available to help and encourage banks "to meet the ordinary continuing or seasonal needs of their established customers, taking account of the special needs of small business, farmers and others." However, the program was limited in two ways. Access to the System's discount facilities were "generally limited to banks with deposits of less than $100 million." Second, to qualify for assistance, a bank would have to have a loan-to-gross-deposit ratio of greater than 68 percent. I think that is another drawback.

These limitations mean that inner-city minority communities will not be helped by this program. This is because inner-city minority communities generally are serviced by branches of banks with deposits far in excess of $100 million. Moreover, small banks that do service inner-city minority communities, including minority-owned banks, generally have loan-to-gross-deposit ratios of 50 to 55 percent, far below the 68 percent set by the Federal Reserve.

Sadly, what we have here is one more example of Government helping almost every community except those where America's minorities work and live. This is not right and it is not fair.

Ways must be found to assure that the continuing and seasonal credit needs of minority communities are met. Both Government, including the Federal Reserve, and the private sector have roles to play. Most important, we must be sure that minority enterprises are able to buy insurance at reasonable rates, for without insurance private sector credit is difficult to get. And also, ways must be found to encourage the flow of equity capital into minority communities under minority management.

This hearing has been called to explore how to get the job done. We will have further hearings on the subject as time passes. For sure, we are going to find out how to do the job.

I would like to indicate and reiterate and reemphasize that unless something is done for minority businesses and is done significantly and quickly, I would expect to see at least a 20-percent loss of minority businesses. They will simply go out of business over the next 2 years. They need special help.

Our witness today is the Honorable Nancy H. Teeters, Governor of the Federal Reserve Board. It is very good to see you again. It was my pleasure to work with you while you served on the House Budget Committee. It was also my pleasure to see you on my recent visit up to the Federal Reserve. We are delighted you could take time to be with us.

STATEMENT OF HON. NANCY H. TEETERS, MEMBER, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

Governor TEETERS. Thank you, Mr. Chairman. It is a delight to be back on the Hill.

Chairman MITCHELL. Would you excuse me just a moment? Mr. D'Amours, do you have a statement?

Mr. D'AMOURS. No.

Chairman MITCHELL. I am sorry. I meant to call on the Congressman to see if he had a statement to make; and he does not.

Governor TEETERS. I appreciate this opportunity to present the views of the Board of Governors concerning steps that might be taken to help meet "the credit needs of inner-city minority communities". The Board commends the subcommittee's efforts to develop means for encouraging an increased flow of credit to minority communities, but believes that use of the Federal Reserve discount window is not an appropriate device to accomplish this purpose. Among the alternatives that are available for promoting the subcommittee's objectives are various proposals to establish special purpose development banks. A more modest but highly effective program with which the Board is especially familiar is the work of the Neighborhood Reinvestment Corporation. The Board recommends that consideration be given to expanding this latter program and through it the activities of local neighborhood housing services corporations and Neighborhood Housing Services of America.

Before turning to a discussion of such proposals, however, I would first like to explain why use of the discount window is not an effective instrument for helping to meet the credit needs of inner-city minority communities. In your letter requesting the Board to testify, you alluded to the fact that the temporary seasonal credit program introduced by the Federal Reserve in April has not been helpful to such communities. This result is not surprising since the special credit program was designed for a different purpose.

As spring approached, the Board had been receiving reports that borrowers in some smaller communities were facing an especially severe financial bind because the local banks on which they depended for short-term credit were fully loaned up. Since farm communities, in particular, were then moving into the part of the year when their seasonal credit needs were largest, there was some risk that lack of financing would curtail planting and subsequently aggravate the inflation of food prices. Although bankers' concerns about loan risk were probably more responsible for their reluctance to meet loan demands than an exhaustion of fund availability, the Federal Reserve introduced the temporary seasonal program to make sure that smaller banks with high loan deposit ratios would have access to loanable funds if they needed them.

Banks serving inner-city communities do not generally fit the specifications of this temporary seasonal program. In particular, the average term of inner-city credit needs is usually a good deal longer than the 6-month maximum maturity allowed under the program. In addition, the primary banking outlets for inner-city areas are branches of banks that are larger than those eligible for the special program. Finally, even the smaller inner-city banks that do meet the size test for the program fall short on the loan deposit ratio test because they face less pressing loan demands.

Looking to the future, the Federal Reserve has not yet completed its plans for administering the discount window after July 1 under the broader lending requirements of the new Depository Institutions Act. While a program for providing seasonal credit will undoubtedly be continued, it is not likely that any practicable program of this type would be especially helpful to banks in inner-city communities,

since it would need to be pegged to a fairly significant regular seasonal pattern of need for funds.

Looking beyond the question of temporary needs for funds, your letter also states that "ways must be found to assure that the continuing credit needs of minority communities are met." You do not indicate whether, or in what way, you believe the Federal Reserve discount window might help to meet such needs. But others have been less reticent in recommending Federal Reserve action. They have urged the Fed to lend to private financial institutions at below-market interest rates. Under this prescription funds provided by the Fed would then be relent to eligible inner-city borrowers—also at less than full market rates, but with an appropriate add-on to cover the private lender's servicing costs and loan risk. Over the years we have had many similar requests from other groups at times of cyclically high interest rates. For example, in the current year alone we have been approached with earnest requests of this type from highly vocal groups representing—in addition to those concerned about inner-city housing needs—groups urging Fed lending at subsidized rates to farmers, homebuilders, other small businesses, and businesses seeking funds for capital expansion.

The Federal Reserve has consistently opposed use of its discount window to provide Government credit to special groups at subsidized interest rates. If this approach were adopted, the demand for subsidized Fed credit could be expected to mushroom dramatically. Unfortunately, the resulting heavy expansion of borrowing from the discount window would risk serious interference with the basic ability of the Federal Reserve to manage monetary policy and thus could prove to be highly inflationary. Moreover, the Fed would be drawn into the highly politicized process of allocating subsidized credit among competing interest groups. Choices of this type clearly should be the function of Congress working through the regular Federal budget process, and should not be delegated, through what would amount to a back-door deficit financing arrangement, to an appointive body like the Federal Reserve.

In contrast to credits advanced by other Federal lending agencies, funds released to the economy through the Federal Reserve discount window are high-powered dollars. They add directly to the reserves of the banking system and provide the base for a multiple expansion of the supply of money and credit in the economy. Also, the initiative in deciding how many of these high-powered dollars are released through the discount window rests essentially with the borrowers, not with the Fed.

In the past the Fed generally has been able to use open-market sales to counter any unwanted fluctuations in the supply of bank reserves that developed from the demands of member bank borrowers at the discount window. But this success has reflected the rather stringent rules that now govern borrowing at the window. Generally, these rules require the borrower to repay the Fed within a short period. For large commercial banks, borrowings from the Fed typically run for only 1 day. While smaller banks may borrow for longer periods—particularly under the seasonal credit program—they too generally make repayments relatively quickly. As a result, both the size and volatility of reserves released to the banking system through the dis-

count window have been kept within manageable bounds. Any program of long-term Fed lending at below-market rates, would risk a serious erosion in this ability to control the volume of bank reserves being released through the discount window. To the extent this happened, there would be an equally serious erosion in the Federal Reserve's capacity to work effectively against inflation.

Moreover, because of the fungibility of money, it would be virtually impossible for the Federal Reserve to monitor the subsidized funds provided through the discount window to assure that they were being used to finance the social purpose for which they were intended. Any serious efforts to try to monitor such lending would require a substantial staff for surveillance and would create a heavy bureaucratic burden on both the conduit lenders and the ultimate credit users. Finally, the Federal Reserve does not now have the statutory leeway to establish a preferred discount rate below the basic rate. The Board, therefore, believes that it would be a mistake for it to mix responsibility for what might become a potentially diverse and sometimes conflicting array of special discount window programs with the broader and overriding Fed responsibility for the conduct of monetary policy.

Of course, a wide variety of Federal and State Government tax incentive and direct subsidy programs already exist that are designed expressly to allocate credit to high priority social purposes. Since these programs have expanded sharpy over the years, they tend to exert pressure on scarce resources. Fortunately, in view of the longer-run need to bring U.S. inflation under better control, the new Federal credit budget became operative in the current fiscal year. For the first time, it now sets a limit on total credit extended through Federal programs and thus establishes the need to allocate scarce credit among alternative uses.

Within this allocation framework, it may now become more dificult to establish new lending programs for such things as urban development, since this may involve trimming an older more established program to make way for the new. Nevertheless, since the need for overall control of credit programs is clear, it is now simply more necessary to make clear that financing of urban development should have a high priority.

The Nation's experience with various attempts to promote urban development, and more specifically, to reverse neighborhood decline indicates that neighborhood revitalization is indeed a complex problem. To be successful, a cornerstone of any such effort must clearly be the provision of a stable source of preferably low cost, long-term funds. In addition to those now pending in the Congress numerous proposals have been made in the past to create an urban or community development bank. The Board feels that these proposals merit special consideration. In addition, it would be willing to lend its expertise, if needed, to support the planning for such a facility, similar to the support for minority banks now being provided under the minority bank development program in conjunction with the FDIC, the OCC, and the Commerce Department. However, in addition to the ready availability of funds, experience indicates that successful community development efforts can be effective only with coordination, involvement and commitment of both time and re-

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sources by local residents, local governments, financial institutions and businesses. Such efforts require the identification of potentially viable programs and projects tailored to meet local needs. Special expertise and knowledge are needed to manage programs and projects to insure their successful completion. Finally, continual monitoring of these programs is required to guarantee that the objectives are met.

For the past few years Board members have served on the Board of Directors of the Neighborhood Reinvestment Corporation—NRC—and its predecessor, the Urban Reinvestment Task Force. Our experience with this Corporation's activities and the local neighborhood housing services—NHS—corporations it develops and assists suggest that they show considerable promise as tools to foster community reinvestment.

One of Neighborhood Reinvestment's most successful activities to date has been to aid the formation of local NHS's which have embarked upon numerous activities to revitalize and refurbish intercity housing. At the heart of each NHS corporation are four key elements that have been pulled together, usually through the initial educational efforts of Neighborhood Reinvestment. These include a core of local residents willing and able to provide the leadership in forming the local NHS corporation; a responsive local government willing to play a role in the NHS activities; a group of financial institutions wishing to participate in supporting the NHS operating budget; and a revolving loan fund administered by the local NHS that is designed to help meet the credit needs of nonbankable NHS clients. Each NHS is run as a nonprofit corporation with a professionally trained staff experienced in running community development projects. They answer to the coalition of local residents, local governmental officials and lenders who sit on the board and participate in the oversight of the NHS's.

Neighborhood Reinvestment's NHS programs have been unique in that rather than relying on Federal outlays to provide the bulk of the funds for reinvestment, they have secured most of the funds for reinvestment from private financial institutions, local governments and other sources. In this way, Neighborhood Reinvestment has been able to leverage substantially the Federal outlays that have been used to get NRC programs started. Over the first 5 years Neighborhood Reinvestment's predecessor, the Urban Reinvestment task force, for example, with $19 million in appropriated Federal funds produced an estimated $32 million in support of local NHS activity and an excess of $119 million in private reinvestment. Many of the newer projects promise reinvestment leverage ratios substantially higher than this. Admittedly, the total reinvestment generated by Neighborhood Reinvestment activities to date is modest, but this reflects the early demonstration scale and the results of the pilot projects. Once many of the pilot projects enter the replication phase across other communities, it is expected that total reinvestment will accelerate substantially. To date, the Neighborhood Reinvestment Corporation has developed and assisted programs in more than 90 cities serving more than 112 neighborhoods.

Although formed under the auspices of the Neighborhood Reinvestment Corporation, local NHS corporations are not primarily financed by Federal funds. They rely on local contributions and grants for their

operating funds and for their revolving loan funds. This private support, along with the active involvement of lenders and neighborhood residents on the NHS boards, is the source of the programs' vitality. The local programs are assisted in obtaining financial institution involvement by the Federal financial regulatory agencies. For instance, Federal Reserve bank presidents help convene the commercial banks in each new NHS development and encourage their participation in the program. They also assist operating NHS programs by convening bankers to hear annual progress reports and to encourage them to continue their annual contributions to the NHS operating budget. During coming months, the Board along with other Federal financial regulators will continue their support through this period of economic uncertainty to insure that the programs' neighborhood activities are not diminished just at the time of greatest need.

Recent high interest rates have placed growing pressure on the NHS revolving loan funds which serve "unbankable" homeowners. Neighborhood Housing Services of America operates a small secondary market for the NHS revolving loan funds. Grants for initial capitalization and interest subsidies provided by the Neighborhood Reinvestment Corporation are leveraged more than 2½ times in sales to institutional investors of notes collateralized by NHS loans. Exploration of enhancing this secondary market would be particularly worthy of congressional attention.

Another critical area worthy of support is the training activity of Neighborhood Housing Services of America. It seeks, in conjunction with Neighborhood Reinvestment, to identify, recruit, and train management to operate NHS's. As with any successful program competent management is always the key. To foster rapid expansion of NHS projects it is necessary to provide an ever increasing pool of qualified people to insure success. For this reason, high priority should be given to supporting this function.

The Board expects in the wake of passage of the Community Reinvestment Act—CRA—that many more financial institutions will be participating in NHS and other Neighborhood Reinvestment Corporation projects. Certainly, expanded participation in these projects will be viewed favorably by the Board when assessing a bank's CRA performance. Furthermore, participation will be encouraged by our bank examiners when they perform their CRA examinations, since the CRA emphasizes that institutions are to make funds available to their local communities, consistent with safe and sound banking practices. NHS programs, to the extent that they employ revolving loan pools to make the nonbankable loans to reduce the risks to financial institutions by engaging in tandem financing, are especially consistent with the objectives of the CRA. For this reason the Board believes that substantial untapped potential remains for additional leverage of Federal funds to provide for further community reinvestment.

In summary, in addition to giving close consideration to the proposals to establish special purpose development banks, the Board would encourage continued support of the Neighborhood Reinvestment Corporation and consideration of methods to expand the availability of appropriated funds to support its development and assistance to local NHS'. Aid should also be provided to support expansion of the local and national revolving loan pools and secondary market activities

as particularly effective ways to promote community development. This policy offers several advantages. The neighborhood reinvestment programs encourage private sector involvement of financial institutions to make the bankable loans rather than relying on straight Federal subsidies. The programs provide for substantial leverage of Federal funds as distinct from purely inflationary Federal subsidies. The programs are easily targeted to specific projects and areas with the greatest need and prospects for success. The programs are carefully monitored. They typically involve projects that provide minimum displacement of local residents. Finally, because of the structure of the programs, they permit a cost-benefit assessment that is not possible with indirect subsidy programs such as those that might potentially be implemented by providing special access to the discount window.

Chairman MITCHELL. Thank you very much. That is very comprehensive testimony. In the middle of it I realized that I had made a mistake. I should never have lumped these two together. What is being accomplished in community development is of some significance, not nearly enough; but the mistake was to have lumped minority business into community development, because—let me try to point out why I say this.

I would suspect that the Board might have a different perspective if we were dealing just with business alone, rather than the totality of community development. It is clear that the Board policies throughout the years have been directed toward business in one way or the other; and I wonder if we had treated minority business as a separate entity in this hearing, whether or not your posture would have been the same.

The sum total of your posture right now is, as I understand it, that really there is no role for the Federal Reserve to play in this problem in terms of its own apparatus. Rather, it sees a role to be played of being supportive of or complementary to other existing mechanisms. Is that generally the sum and substance of it?

Governor TEETERS. Mr. Chairman, as I was thinking through this testimony, it seems to me the role of the Federal Reserve is that of a central bank. Generally speaking, the central bank does not allocate credit. Our temporary seasonal program announced earlier this spring was to assist banks in smaller communities that were under severe liquidity pressure and had no effective access to national money markets.

Most publicly supported credit allocation in the United States occurs through guarantees. The guarantee credit program—as you well know—has proliferated outside the entire budget operation to assist agriculture, housing, students, and to help meet other special needs.

That is the mechanism through which special credit needs are and should be accommodated rather than through credit created by the central bank. The Federal Reserve is prepared to lend its expertise to other agencies to assist in developing viable lending programs, both at the Board here in Washington and through our Reserve banks in other parts of the country.

But basically our job is to control the creation of money not to allocate credit.

Chairman MITCHELL. I hear you. But I am not at all sure that I am in full agreement. Let me try it this way.

The Fed moved in in terms of smaller communities, with farmers, with the seasonal program. I have some problems—there are problems that occur during a season which warrant your involvement. On the other hand, the reference to minority businesses that have almost the same kind of problem for businesses as you have for minority unemployment.

I am talking about a structural problem; and I am a little hard put to accept the version that the Fed would have no role to play in attaching a structural problem that effects minority businesses.

Could I just sort of illustrate for you the nature of that structural problem? Historically and traditionally minority enterprise has had an enormous difficulty in terms of access to capital. Historically and traditionally, despite a 90-percent guaranteed bank loan program by the Small Business Administration, banks do not lend to minority businesses. In general, they just don't.

So you have a long-term structural problem that has all of the features—it seems to me—of the seasonal problem that you are dealing with.

Governor TEETERS. Let me make one comment on the seasonal program. That was introduced in early April. Only about 75 small banks—between 75 and 100 small banks—have negotiated agreements with the Reserve banks to access this credit. To date, very little of that money has been taken down. There are credit lines established, but they actually have not drawn on it very much, so that use of that program has not been very large at this point.

The problems of small businesses, minority businesses, and women-operated businesses are, I think, the longstanding ones of bankers not recognizing where their best interests lie.

The Community Reinvestment Act is now helping to provide a fuller bank review of such options by requiring bankers to define their community and report the type of loans they are making to it. We have established a separate examination force to check on the results.

Chairman MITCHELL. Can I ask a question on that point?

Governor TEETERS. Yes.

Chairman MITCHELL. Would not a bank meet all of the requirements of that program if it would lend money solely to housing development? It would have reinvested in the community in, say, a fair share?

Governor TEETERS. Actually, in the few cases where there have been protested applications, review of the lender's performance has looked not only at housing loans but also at loans to business in the geographic areas the lender has said it is servicing. Admittedly, the housing data are a little bit easier to collect, but our examiners are also looking at the portfolio of loans to businesses to see that it, too, is meeting the needs of the community.

Chairman MITCHELL. Under present guidelines, if a bank should lend $10 million to the community, all $10 million of that went into some kind of housing development program or programs, would it not then satisfy requirements?

Governor TEETERS. I don't think so, because the act requires that the bank state the type of loans that it is making available to its community; and they can exclude housing. There is nothing that says they have to include housing in there. In some cases where you have

large wholesale banks, they have done that; but if the bank says they are making available loans to small businesses, then our examiners will look to see that they are truly doing that. In other words, the only way a bank could meet the CRA as you have described it is if it announced that housing loans were the only ones it was making available in its local community.

Chairman MITCHELL. You see, you are getting at the very point I was trying to get to. It is possible under the program then for the lending institutions to lend all of their money to small businesses, in general, or to housing, or a combination thereof and exclude minorities. They can exclude minority business. They would still be meeting the requirements of the legislation.

Governor TEETERS. As you know consumer legislation applies to a number of different programs and equal opportunity credit is just one part. But the examiners of lender performance are checking for compliance with all such legislation.

So if it is not community reinvestment, it will come under equal opportunity credit. This examination force is about 15 months old. It has the special function of helping regulatory agencies make sure that their regulatees are complying with the full range of laws. If the banks are making loans to small businesses, they cannot exclude "minority" small businesses.

Chairman MITCHELL. I will surely follow up on that, because——

Governor TEETERS. I am following it, too.

Chairman MITCHELL. My own experience has been so bad in terms of the lending institutions and minority businesses, I am not at all sure this new structure is going to address that problem.

Let me shift from that to—we always get into these philosophical discussions. In the latter portion of your testimony—I don't recall the page exactly—you said that—I think the quote was "purely inflationary Federal subsidies."

Governor TEETERS. I did say that. I sort of stumbled on it, also.

Chairman MITCHELL. What?

Governor TEETERS. I sort of stumbled on it, also.

Chairman MITCHELL. Just in our little 2-minute philosophical discussion, are you suggesting that all subsidies by the Federal Government are purely inflationary?

Governor TEETERS. No, sir. I think it depends a great deal on how the programs are implemented. I particularly want to urge that you give serious consideration on the national credit budget, because I think without some overall control of this type credit programs can represent a serious loophole in the budget process. These are some older credit programs which might well be phased out at this point to make room for newer more urgent programs. A national credit budget will require Congress to list priorities in deciding such questions.

I am not attempting to say that all credit programs are purely inflationary. Certainly subsidized credit is a legitimate way for Government to help direct private economic activity.

The problem, as you well know, with the budget process is that totals tend to get too large if Congress doesn't consider the overall economic impact of the budget and, where necessary to control this impact, make choices between alternative programs.

Chairman MITCHELL. OK. I am glad you cleared up my mind on that.

Also on page 4, there was a statement that perplexed me a little bit. The second paragraph toward the end:

> Any program of long-term Federal lending at below market rates would risk a serious erosion in this ability to control the volume of bank reserves being released through the discount window. To the extent this happened, there would be an equally serious erosion in the Federal Reserve's capacity to work effectively against inflation.

Let me tell you why I have a problem with that. Perhaps you can clear it up for me. When you look at the totality of all, let us say, black-owned businesses in America, every business that you can think of, the smallest of the Fortune 500 companies can purchase the total number of all minority businesses and still have a lot of money left over.

The point I am trying to get to is that if you would focus in just on minority businesses, I don't see the amount of money in any way endangering the Federal Reserve's program. You are dealing with such a miniscule amount of the economy.

Could you discuss that for me, please?

Governor TEETERS. Yes; I am sure the same thing could be said for female-owned businesses also. I think we are even a smaller group. However, I did learn one thing in the budget process: That the little pieces add up very rapidly to a very large total.

It seems to me that the appropriate agency to allocate credit to small minorities businesses is the SBA. Credit allocation for social purposes should not be the function of the Federal Reserve since it would inevitably interfere with general monetary policy.

If we begin to open the discount window for one small group, we will quickly be approached by many other small groups, seeking similar assistance outside the Federal budget process. As we found with our program of special credit controls, everybody has a special case to plead. Thus, any willingness of the Federal Reserve to support special needs of this type could result in larger and larger volumes of credit being supplied through the discount window whether or not they were consistent with the needs of general monetary policy at this time.

I really do think that the way to proceed in meeting your problem is through the allocation of credit being supplied through the national credit budget. It's a matter of redirecting Federal loan funds to make sure they are going to the right places.

The Neighborhood Services Corporation, which is very small at this point, has been successful. It is perhaps one of the only really successful rehabilitation programs that we have. It is an amalgam of local people as well as Federal expertise and a minimal amount of Federal money.

Chairman MITCHELL. Let me try it another way. Could you foresee any circumstances for any group which would cause the Federal Reserve in its monetary policy to shift to a microemphasis for that group rather than the macromonetary policy?

Governor TEETERS. As you say, we do get into these philosophical things. I don't think it is the business of the central bank to allocate credit. I really think that our function would be diluted if we got into

credit allocation per se. Federal guarantee programs, starting in the 1930's with housing and agricultural credit, have grown to be the primary form of credit allocation for social purposes in our country, giving people in need a step-up in the line at the credit window.

It seems to me that it would be more appropriate to influence such programs and to change the uses and terms under which they are administered than to impair the function of the central bank.

Chairman MITCHELL. We shall see. It is very interesting. I did not mean to make a joke out of it. It was very interesting that suddenly you see the Joint Economic Committee of the Congress beginning to address microproblems now. That traditionally had not been addressed by them. Some of the standing committees of the House—Ways and Means, other committees—are beginning to address microproblems. I am not at all sure that the Fed can forever stand aloof from directing some of its efforts on a microbasis, that is, minority businesses.

Governor TEETERS. Perhaps, but I still think the other avenue is better and one more directly under the control of the Congress.

Chairman MITCHELL. On page 6 of your testimony, you indicated that you would support establishment of an urban or community development bank. Can we discuss that just a little bit? Would this bank, as you see it, as you envision it, be authorized to make low-cost, long-term loans to businesses? Or to new businesses? Or to small businesses?

Obviously to minority businesses. Could you see this bank confining its loans primarily to cities and minorities?

Governor TEETERS. Mr. Chairman, I must confess I do not know a great deal about your bank proposal. Let me say before I discuss with you what I think it could do, that I don't think such proposals should be considered until you have the credit budget in place.

Chairman MITCHELL. I am sorry.

Governor TEETERS. I think you should get your credit budget into place and then fit the credit programs together rather than simply to spinoff a new credit program that is not part of an overall view as to how an appropriate overall credit total should be allocated.

Essentially in the past we have spun off a large number of guaranteed credit programs without really focusing on their overall implications for the economy.

In developing the Urban Redevelopment Bank, I think we need to review other programs already in place. One of the largest guaranteed programs is the FHA support for housing. As I remember the proposals for Urban Redevelopment Bank, they were primarily to provide credit for the redevelopment of the inner cities. There is no reason why support for inner-city small business could not be included in such a program, in addition to the programs of the Small Business Administration.

In putting together an Urban Redevelopment Bank program it seems to me that it should focus not only on new credit programs for the urban areas, but should also round up some of the existing programs and integrate them into a comprehensive program for center city redevelopment.

Chairman MITCHELL. I understand. It is a bad day for me, because 10 years I have been here. I have seen programs develop, designed for the cities and so forth. Take, for example, the community development block grant program which has been a boon to many cities; but

as I look back over the last 10 years, none of these has a special emphasis for minority business. I am so concerned about that, because quite frankly I see the erosion or the demise of a number of our human resources programs as evidenced by this ridiculous budget cutting that is going on right now.

I think there has got to be something viable in our communities to substitute for those programs that are going to be eroded or lost to us. The only viable thing would be minority business. Yet, in a decade, I have not seen any one thing except a small portion of the SBA—Small Business Administration—I have not seen any tangible specifically targeted governmental efforts for minority businesses.

Could I ask you just one other question? You say look at your credit allocation first and then fit this in. But on page 6 in your testimony you indicate that with reference to an urban or community development bank, the Board feels these proposals merit special consideration. In addition, it would be willing to lend its expertise, if needed, to support the planning for such a facility. Could I take that to mean that we could get back to you if I or some other members of the subcommittee wanted to start drafting some legislation along these lines, that you would help us to develop such a legislation?

Governor TEETERS. Certainly. May I point again to the Neighborhood Service Corporation? Granted, it is small. But it was started as a pilot project. The thing that truly impresses me about it is that it has been successful; and the prototype of involving local people, local governments, and providing expert managers who, incidentally, are selected by the local people. Even though this program is small, it is now expanding. As a prototype of a successful program, it should be very carefully looked at as something that can go into an area and actually work. We have had so little success in some of these areas.

This is one in which all of the essential ingredients of a successful program have come together. I am really impressed with it.

Chairman MITCHELL. I know the program. I must confess I have not studied it deeply. I would be very curious to look at the extent and the degree to which minority businesses have been an integral part of this program.

You see, you can do community reinvestment, community development and actually you can do it by totally excluding minority businesses.

Governor TEETERS. I have just been told this neighborhood approach was started to provide support for housing. But a new organization has also been developed on a pilot basis to promote commercial development within inner-city areas. It is directed toward the upgrading and rehabilitation of commercial areas within a given neighborhood. This assistance extends to businesses, particularly small businesses, in the neighborhood areas.

Chairman MITCHELL. Yes; but not necessarily minorities. You see, the point is: You can take the deepest ghetto in the world and have one of these groups move into commercial development. It can be really a business that is located on the perivy of the city which would come into——

Governor TEETERS. I don't think that's so.

Chairman MITCHELL. Under commercial development, this could be done.

Governor TEETERS. I think they are looking more at the neighborhood shopping areas.

Chairman MITCHELL. Sure they are, but could we construct that neighborhood shopping area—that could be done—the construction of it could be done by a business far removed from the area. The ongoingness of it would rest with the community.

Governor TEETERS. One of the good things about this program, particularly in the housing area, is that it has not displaced residents. There has not been the problem of having to move people out in order to rehabilitate. I offer this as a suggestion because it is something that is functioning. It is something that is a new way of approaching the problems of the inner city and one which has involved—and apparently this is extremely important—the people in the area plus the local governments.

Chairman MITCHELL. Let me shift gears. In my opening statement I remarked about the difficulty minority businesses have with insurance. It is a problem for, I guess, all businesses in urban areas, but it is an exasperating problem for minority businesses. What would you think of maybe a fiscal program, not monetary, whereby the Government picked up directly a substantial part of the insurance costs for businesses located in inner-city communities? Would that be a purely inflationary subsidy? What about a program whereby the Federal Government picked up a substantial part of the local property taxes, on business properties, in inner cities to help subsidize this?

Governor TEETERS. I would still rather see it wrapped up in a program like NHS. One of the problems with insurance companies is that most of them are regulated by the States. This creates a problem for any sort of Federal program. We do have, as you well know, flood insurance federally. If you looked to that program for guidance, it might provide insights on how insurance might be provided to cover some of the special hazards of inner-city operations.

That's the only Federal insurance program of that type that I think I know of.

Chairman MITCHELL. Well, I guess I am just too biased and nonobjective in my thinking. In my own thinking, the problems of monority businesses amount to a disaster; and if we can come up with a disaster loan or come up with a special seasonal loan for rural farm areas, then I just fail to see why we can't grasp the significance of the dimensions of the minority business problem. You made it very clear to me that the Federal generally would not intervene directly in this; that has been your consistent position.

Governor TEETERS. We do not want to get involved in the allocation of credit per se.

I still think that you can develop a more effective approach through Federal guarantee programs and a comprehensive urban bank—with particular emphasis on ways to develop the local expertise needed to carry out programs at the local level.

Chairman MITCHELL. Two last questions from me. What, if any, was the Federal Reserve Board's involvement in the Chrysler loan? Did it plan any role at all?

Governor TEETERS. The Chairman specifically was appointed by Congress to help evaluate the loan proposal and certify whether it would be workable.

Chairman MITCHELL. Do you know whether the Chairman felt there were any adjustments to be made in monetary policy because of the loan to Chrysler?

Governor TEETERS. No, because the loan is provided from Treasury funds and taken down over a very long period of time.

Chairman MITCHELL. Well, I guess I didn't get very far, did I, Governor?

Governor TEETERS. I think we did, though, Mr. Chairman. I think your major thrust should be to put together a viable program aimed at the inner cities with as much local participation as you can get, and with as much expertise in the administration of the program. One problem in expanding the Neighborhood Services Corporations is in getting really good project directors who know what they are doing. But there is a framework here that has worked and that could be expanded. We don't want to expand it so fast that it breaks down; but it is the type of program which I believe provides the best hipe for coping with such problems in the future.

Chairman MITCHELL. You are right. We did have significant discussion with regard to neighborhood community development. I have to go back to my original statement where I said I made a mistake. I do not want to treat minority business as part of general neighborhood development any more than you would consider Ford as a part of general neighborhood development. I am trying to move to a point where neighborhood businesses stand as any other business in this Nation.

It is at that point where I do not think we have gotten very far.

Governor TEETERS. Again, I would say that by making sure that the laws on equal opportunity in credit are enforced, we will be making a start down that road.

Chairman MITCHELL. Thank you very much. You have been very patient with me. Congressman Ron Paul has arrived. Do you have any questions?

Mr. PAUL. Thank you, Mr. Chairman. I would like to ask one brief question. I realize it is not directly under the Federal Reserve Board control but rather under the Comptroller. Could you tell me how many banks that are minority controlled hold charters? Do you know that?

Governor TEETERS. About 90 banks that are minority controlled.

Mr. PAUL. Do you know if there has ever been a problem or complaints about minorities being able to get these charters? Do we know what percentage that would be, what percentage is that for all bank charters? These are Federal bank charters you are talking about?

Governor TEETERS. I think the 90 covers all, Federal and State.

Mr. PAUL. What percentage would that be?

Governor TEETERS. There are 14,000 banks.

Mr. PAUL. 90 out of 14,000?

Governor TEETERS. It is a very small percentage.

Mr. PAUL. Does the 90 include women?

Governor TEETERS. Yes. That includes women's banks, too.

Mr. PAUL. What?

Governor TEETERS. Women's banks.

Mr. PAUL. Women's? Thank you.

Chairman MITCHELL. I think on that chuckle this is an appropriate time to say the hearing is now adjourned. Thank you very much, Governor Teeters, for being with us.

[Whereupon, at 10:50 a.m., the hearing was adjourned subject to the call of the Chair.]

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